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The Millennium Challenge Corporation, law, and poverty reduction

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> The Millennium Challenge Corporation is "... designed to contribute to fighting poverty in a way that will make the world more secure – by creating an incentive for good governance and by helping countries take effective control of their own development."
>
> Secretary of State Condoleezza Rice (2004)[1]

16.1 Introduction

The Millennium Challenge Corporation was created by the US Congress in 2004. It is an independent and innovative US foreign aid agency with an annual budget appropriation that has averaged $1.2 billion since 2004. A Board of Directors chaired by the Secretary of State oversees MCC operations. Other board members are the Secretary of the Treasury, the USAID Administrator, the US Trade Representative, MCC's CEO, and four private sector representatives. MCC provides large grants, "compacts" in MCC parlance, to a small number of eligible developing countries. To date, twenty-five compacts, averaging over $350 million per country (and ranging from $66 million in Vanuatu and Cape Verde to $698 million in Tanzania), have been signed. MCC delivers smart aid through its focus on good policies, country ownership, and measurement of results.

MCC is distinctive in several ways. Only a small number of developing countries can receive MCC grants. Selection is competitive, and MCC's board examines performance on twenty independent and transparent policy indicators. MCC requires selected countries to identify priorities

* The views expressed are the author's own and do not necessarily reflect the policies of MCC.

1 Millennium Challenge Corporation, "Annual Report" (2004). Secretary Rice also served as the Chair, MCC Board of Directors.

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for development through a constraints analysis. Countries must also conduct national consultations to confirm broad support throughout society for their proposed program. The evaluation of proposed projects includes calculation of an Economic Rate of Return and its impact on poverty reduction. Each country administers its own grant through an accountable entity, often referred to as an "MCA" (from Millennium Challenge Account). Procurement is untied, and open to international competition. Finally, Compact activities are designed to exhibit a very high level of transparency and include extensive monitoring and evaluation throughout the five-year life of a compact, and beyond. Countries can, and have, lost funding in mid-compact for failure to maintain performance levels.

The connected, twin goals of MCC are poverty reduction through economic growth. MCC selection and programs may not be directly connected with matters of international economic law, however, the norms of national laws and policies, and how they impact development are at the center of the MCC experiment. This chapter briefly examines how MCC's legal and policy focus seeks to impact economic growth and poverty reduction.

16.2 Law, policy and selection – economic growth and poverty reduction

Most distinctive among the MCC processes is its use of policy indicators to identify potential compact countries. The board examines whether a country performs above the median compared to income peer group countries (low income countries or lower middle income countries).

To win the opportunity to negotiate a compact, a country must score above the median in at least half of the twenty indicators utilized in an MCC "scorecard." For an example of a scorecard, see Figure 16.1, "Fiscal year 2012 MCC country scorecard for Ghana."[2] In addition, a country must rise above the median on the Control of Corruption indicator. Beginning in fiscal year 2012, countries must also score above the median on either the Political Rights or Civil Liberties indicator before they are invited to develop a compact. Even then, the opportunity to develop a compact remains at the discretion of the MCC board. In an effort to de-politicize country selection for compacts, none of the indicators used is produced by the US Government. All indicators are developed by

2 Ghana has successfully completed its first compact, valued at $547 million, in February 2012, and is negotiating a second compact.

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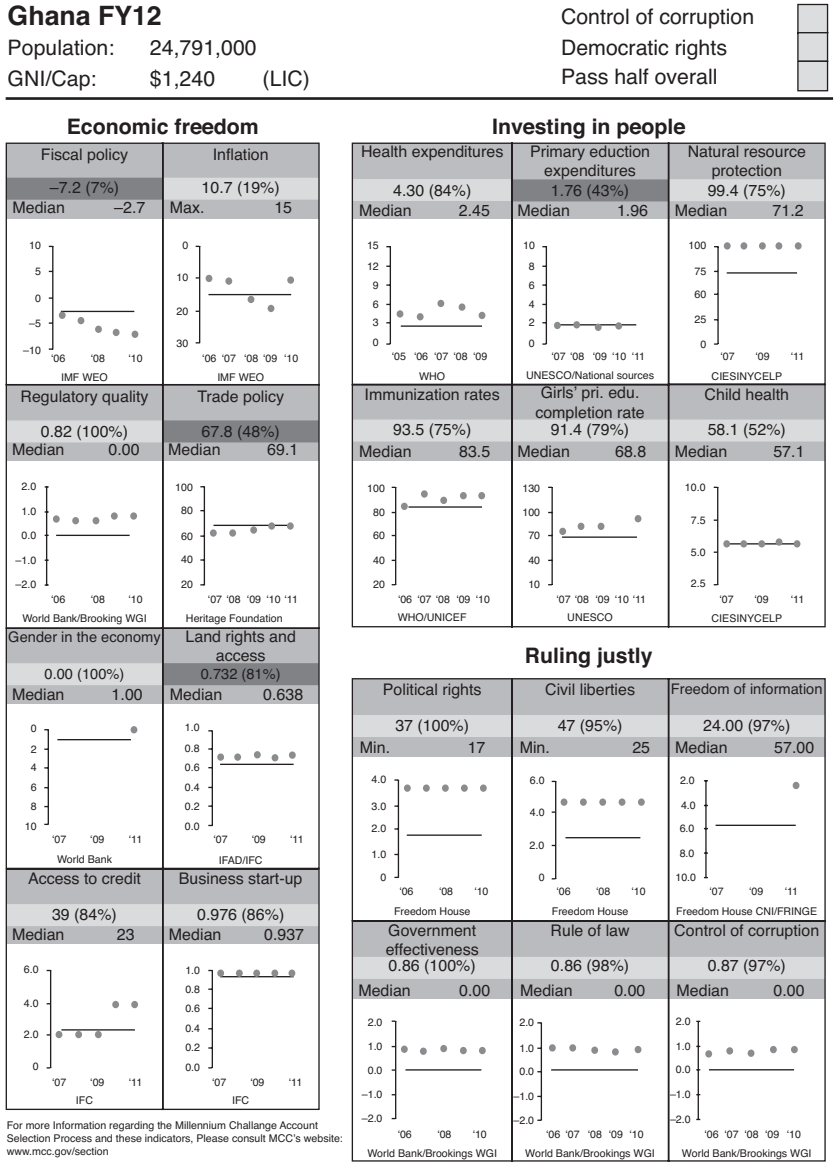

Figure 16.1. Fiscal year 2012 MCC country scorecard for Ghana

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international organizations (including the World Bank and UNESCO) or non-governmental organizations (such as Freedom House and The Brookings Institution).

The indicators are divided into three groups: Economic Freedom, Investing in People, and Ruling Justly. The "Guide to the MCC Indicators and Selection Process for Fiscal Year 2012"[3] provides a detailed description of the indicators, their sources, and rationale for MCC's use. Note that most of the indicators focus in one way or another on the mediation between a government's obligations and an individual's or the broader society's rights, as defined by law. In indicators such as "Gender in the Economy,"[4] "Natural Resource Protection," or any of the indicators under the heading "Ruling Justly," the individual indicator examines the laws surrounding those issues; the application of policies, laws, and regulations; their enforcement, and their impact on individuals. The "score" is then derived by comparison with the performance of peer countries. We will briefly examine a couple indicators to illustrate the direct connection between law, economic growth, and poverty reduction that is implicit in MCC's selection and use of indicators. For example, the "Gender in the Economy" indicator – among MCC's newest – " . . . measures the government's commitment to promoting gender equality by providing women and men with the same legal ability to interact with the private and public sector."[5] The indicator examines twenty activities (such as the ability to start a business and enter into a contract – and whether women are in any way legally disadvantaged compared to men). MCC has included this indicator because numerous studies have shown that laws sanctioning gender inequality in economic matters negatively impact economic growth and poverty reduction. Likewise, MCC utilizes the Natural Resource Protection indicator explicitly because of the connection between good laws and policies in this area and economic growth and poverty reduction. The protection of biomes and ecosystems is shown to positively impact long-term economic growth. Within the indicator grouping Ruling Justly, probably the most significant of the three pillar groupings as it includes the most "must pass" indicators, the legal aspects are more obvious even if the economic impact may not always be self-evident. However in each case – from

3 MCC, "Guide to the MCC Indicators and the Selection Process for Fiscal Year 2012," www.mcc.gov/documents/reports/reference-2011001066102-fy12-guide-to-the-indicators.pdf.

4 World Bank, "Women, Business and the Law," http://wbl.worldbank.org.

5 See MCC, "Guide to the MCC Indicators," p. 40.

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Political Rights to Freedom of Information – an explicit connection between the indicator, economic growth, and resulting poverty reduction has been established. For a more lengthy and interesting discussion of the connections between democratic rights and economic development, see "MCC and the Long Term Goal of Deepening Democracy."[6]

16.3 The MCC compacts – less law and policy, more physical infrastructure

To date, the preponderance of funding has – as requested by recipient countries – been allocated to large infrastructure projects such as roads and power. Considering the size of the compacts and the favorable terms – grants, rather than loans – it is understandable that countries would prioritize infrastructure projects, rather than focusing on policy-focused activities. MCC policy-oriented reforms are largely embedded in projects. Non-MCC funders such as the World Bank and USAID, with much larger budgets, project oversight capacity, and broader subject matter expertise tend to take the lead on law- and policy-related project activities. A very small percentage of MCC funds under the compacts support projects in areas such as land rights and judicial administration. However, government policy within MCC-funded sectors, such as regulatory issues in power, is increasingly a consideration in compact design.

16.4 Threshold programs – strong legal focus

MCC's threshold programs (averaging a little more than $21 million per country in the twenty-three threshold countries to date) are smaller grants that help countries become eligible for compacts by targeting policy and institutional reforms. Most of the projects have focused on law-related matters such as government procurement, tax and customs administration, judicial reform, trade policy, business registration, government transparency, and land rights. USAID has administered virtually all threshold programs. For more details on the recipients, content, and design of MCC threshold programs, see the MCC website.[7]

6 MCC, Alicia Mandaville Phillips, "MCC and the Long Term Goal of Deepening Democracy" (2007), www.mcc.gov/documents/mcc-112007-paper-democracy.pdf.

7 MCC, "Threshold Program," www.mcc.gov/pages/program/type/threshold-program.

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16.5 Will MCC's legal focus impact policy reform and thus economic growth?

While it is perhaps too early for any definitive answer, early indications of a hoped-for "MCC effect" appear positive. Numerous countries have enacted legal, regulatory, and policy reforms in the hope of improving indicator scores and receiving an MCC compact. Significant policy reforms are also included in some compacts. Some scholars have argued that the long-term economic impact of MCC-incentivized reforms will be more significant in economic terms than the actual compacts.[8] An extensive analysis, and a thorough description of logic for MCC's policy and governance-related work, is provided in "The Millennium Challenge Account: Influencing Developing Countries Through Performance-Based Foreign Aid."[9] The most extensive coverage and ongoing analysis of all aspects of MCC's activities is provided by the Center for Global Development. CGD's online "MCA Monitor"[10] provides regular and up-to-date commentary on all aspects of MCC's activities as well as its impact in compact countries and beyond. Perhaps the most positive recent feedback on MCC's methodology and policy focus was noted in the Organization for Economic Co-operation and Development's recent "United States (2011), DAC Peer Review":

> Through the MCC, the US has shown that it can deliver development cooperation that is in line with the principles of effective aid. In particular, ownership, predictability, untying, unearmarked funding, and a strong emphasis on results are key characteristics of MCC's approach. MCC also provides an incentive model that supports partner countries in their reform: it allocates aid based on a country's policy performance, employing objective indicators to determine a country's eligibility for funding.[11]

8 See D. Johnson and T. Zajonc, "Can Foreign Aid Create An Incentive for Good Governance? Evidence from the Millennium Challenge Corporation," Kennedy School of Government, Working Paper Series (2006), www.hks.harvard.edu/var/ezp_site/storage/fckeditor/file/pdfs/centers-programs/centers/cid/publications/student-fellows/wp/011.pdf.

9 See R. Stubbs, "The Millennium Challenge Account: Influencing Governance in Developing Countries through Performance-Based Aid," *Vand. J. Transnatl. L.*, 42 (2009), 621.

10 See Center for Global Development, "MCA Monitor," www.cgdev.org/section/initiatives/_active/assistance/mcamonitor.

11 OECD, "The United States, Development Assistance Committee (DAC) Peer Review 2011," www.oecd.org/dataoecd/43/6/48434536.pdf.

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16.6 Conclusion: Can we draw conclusions?

It may be too early to draw definitive conclusions about the impact of policy-oriented and performance-based modalities of development assistance such as MCC, and its less-discussed EU analog, the "Development Policy Tranche."[12] However, provision of foreign aid in the absence of effective consideration of the policy and legal context has too often been proven unsustainable and ineffective. It is hoped and intended that MCC's methodical, and policy-based, selection process will show a clear line of progression between better policy performance prior to Compacts (as exhibited by measurable legal and policy performance) and will lead to more successful outcomes – meaning increased rates of economic growth and poverty reduction.

12 See N. Molenaers and L. Nijs, "From the Theory of Aid Effectiveness to the Practice: The European Union's Governance Incentive Tranche," *Development Policy Review*, 27 (2009), 561.

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